Public Law 85-804 Indemnification

The History of Act

Shortly after the bombing of Pearl Harbor, Congress addressed the need to speed up the procurement of war materials. In 1941 Congress enacted the first War Powers Act. The Act permitted the President to enter into contracts "without regard to the provisions of law relating to the making, performance, amendment or modification of contracts" if it would "facilitate the prosecution of the war."

While the Act did not specifically address indemnification of contractors, the Attorney General interpreted the above grant of authority as being without any limitation whatsoever. Consequently, the Attorney General discerned that indemnification of a contractor against loss by enemy action was within the Secretary of War's authority under the War Powers Act.

The authority of the Act was limited to World War II. As a result, when the Korean Conflict began, President Truman asked for legislation like the War Powers Act, which would improve the acquisition of war materiel for a general mobilization. Notably, one of the reasons President Truman requested the legislation was to be able to indemnify contractors performing especially hazardous work. In the event these contractors suffered damage to their facilities or equipment, the facilities or equipment could be replaced right away. Losses resulting from personal injury were not the focus. As there had been no declaration of war, it was no longer necessary to show that it would facilitate the prosecution of war. The revived War Powers Act required that before action was taken it would be necessary to show that such action would "facilitate the national defense".

After many renewals, this legislation continued to be in effect until 1958. Industry lobbied Congress heavily to make the indemnity offered by the War Powers Act permanent. Now industry was concentrated on its losses. It was concerned not only about damage to facilities, but also damage to the company shareholders if even an unsuccessful suit was filed against the company. In its deliberations, Congress considered the enormous claims a company might incur in the event of an accident and the fact that liability insurance was generally inadequate for government contractors.

Ultimately Congress decided that the United States would assume the risk of loss in these instances to the extent private insurance was not reasonably available. In 1958, Public Law 85-804 was enacted. It provided,

"Be it enacted by the Senate and the House of Representatives of the United States of America in Congress assembled, That the President may authorize any department or agency of the Government which exercises function in connection with the national defense, acting in accordance with regulations prescribed by the President for the protection of the Government, to enter into contracts or into amendments or modifications of contracts heretofore or hereafter made and to make advance payments thereon, without regard to other provisions of law relating to the making, performance, amendment , or modification of contracts, whenever he deems that such action would facilitate the national defense."

Executive Orders

A series of Executive Orders implemented PL 85-804. Most noteworthy is Executive Order 11610, issued in 1971 by President Nixon. Essentially, this Executive Order had three purposes. First, it limited indemnity to those situations in which the contractor is exposed to risks that are "unusually hazardous or nuclear in nature." Second, it required that the indemnification be approved in advance by an official at a level not below that of the secretary of a military department. Third, it required that the approving official take into account the availability, cost, and terms of private insurance.

The Request for Indemnification

A contractor requesting indemnification must submit a request to the contracting officer. This request must comply with Federal Acquisition Regulation (FAR) 50.403-1. The request must identify and define the unusually hazardous or nuclear risks for which indemnification is requested, together with a statement indicating how the contractor is exposed to these risks. It must also include a statement of all insurance coverage applicable to the risks to be defined in the contract as unusually hazardous. The contractor must furnish information regarding the availability, cost and terms of additional insurance or other forms of financial protection. This permits the agency to comply with the third requirement of Executive Order 11610.

Action on the Indemnification Request

The contracting officer may deny the request, so long as this is done after consideration of all the facts and evidence and so long as the contractor is promptly notified together with the reasons for the denial. If the contracting officer recommends approval, the contracting officer forwards the request through channels to the approval authority. According to FAR 50.403-2, the contracting officer must prepare a submission which includes, among other things, a definition of the unusually hazardous risks involved in the proposed contract together with a statement that the parties have agreed to it. The submission must also contain a statement that the contract will involve unusually hazardous risks that could impose liability upon the contractor in excess of financial protection reasonably available and a statement by the responsible authority that the indemnification action would facilitate the national defense.

Approval Authority

The approval authority for the Army is the Secretary of Army (FAR 50.201(d)), who approves indemnification by a Memorandum of Decision (MOD). The MOD authorizes the contracting officer to include the indemnification clause in the contract and defines the ìunusually hazardousî risk for which the contractor is indemnified. The MOD may also authorize the extension of indemnity to subcontractors.

Inclusion in the Contract

After the contracting officer receives approval through the MOD, the contracting officer modifies the contract to include the indemnification clause, FAR 52.250-1, "Indemnification Under Public Law 85-804," and the definition of unusually hazardous risks.

The clause indemnifies the contractor against claims by third persons for death, personal injury, or loss of, damage to, or loss of use of property. "Claims" includes reasonable costs of litigation or settlement. This indemnity also covers loss of, damage to, or loss of use of contractor and government property. However, it applies only to the extent that the claim or loss results from the risk defined in the contract as "unusually hazardous" and when the claim or loss is not covered by insurance.

Importantly, the clause excludes loss or damage caused by willful misconduct or lack of good faith on the part of the contractor's principal officials. If the MOD permitted and the contracting officer gives prior written approval, the indemnity may also be extended to subcontractors at any tier. Even if the contract is terminated, expires or is completed, the rights and obligations of the parties under the indemnification clause will survive.

Examples of Unusually Hazardous Risks

At the Industrial Operations Command, contractors requesting and receiving approval of indemnification are those who operate Government Owned, Contractor Operated (GOCO) plants and those performing chemical demilitarization efforts. The Secretary of Army has approved the use of the Public Law 85-804 indemnification clause in certain GOCO contracts since 1972. What constitutes an unusually hazardous risk at these munitions facilities has evolved since that time (especially as the sensitivity to environmental issues has increased), but generally covers two types of risk: explosive and environmental.

The most recent definition of the unusually hazardous explosive risk is the risk of detonation, explosion, or combustion of explosives, propellants or incendiary materials, or munitions containing explosives, propellants, or incendiary materials (collectives, Products during the course of their manufacture, assembly, shipment, storage, treatment, use, disposal, generation, transportation, remediation, or other handling (collectively, Handling).î

The environmental risk to which the GOCO contractors are exposed is currently defined as the risk of release, including threatened release, whether on-site or off-site, sudden or nonsudden, of any substance or material (including Products) the Handling of which is or becomes regulated under law, during the course of their Handling, provided such substance or material was either: (a) present at or released from the facility prior to the contractor's operation of, or Handling at, the facility, whether known or unknown by the Government or Contractor at such time; (b) obtained by or provided to the contractor for incorporation into Products; (c) required by or designated in Government specifications or other relevant technical documentation to support the Handling of products; (d) otherwise reasonably required to enable the Contractor to perform its functions and responsibilities at the facility; (e) generated by the contractor's Handling of products or provided to the contractor by the Government or its agents for Handling; or (f) introduced onto the facility as a result of action by a party other than the contractor or the contractor's agents.

For chemical demilitarization efforts, the unusually hazardous risks are typically defined as the risks of: (a) sudden or slow release of, and exposure to, lethal chemical agents during the disposal of stockpiles of chemical munitions, mines, or other forms of weapons-related containerization and during facility decommissioning and closure; (b) explosion, detonation or combustion of explosives, propellants or incendiary materials during the course of disposal of stockpiles of chemical munitions, mines or other forms of weapons-related containerization; (c) contamination present at or released from an installation prior to the contractor's construction or operation of the chemical

demilitarization facility (CDF), whether known or unknown by the Government or contractor at such time; (d) contamination resulting from the activities of third parties when the contractor has no control over such activities or parties; and (e) contamination resulting from the placement of components and materials from decommissioning and placement of wastes and residues from demilitarization, destruction, or closure in accordance with the contractual requirements and all applicable laws and regulations

There has been some criticism of the use of these indemnification provisions over the years. It has been suggested that insurance to cover these risks may be available. It has also been suggested that the definition of unusually hazardous risk is too broad, covering materials that are routinely used by industry without connection to the national defense. Some risks defined as "unusually hazardous" are assumed every day by commercial contractors operating their own facilities.

However, the contractors consistently report that insurance for environmental tort or cleanup costs is unavailable at any price. Furthermore, the GOCO operating contractors maintain that while they or others may operate commercial facilities without insurance for risks of environmental releases, they do so earning a higher rate of profit than under a GOCO contract.
Despite this criticism, the Secretary of Army continues to approve requests to include the indemnification clause in Industrial Operations Command contracts (issuing a GOCO MOD as recently as October 1998). While the risks considered to be "especially hazardous" or "unusually hazardous" have evolved greatly since the War Powers Act of 1941, it appears that the Army policy remains to be that the use of Public Law 85-804 serves a valid purpose and should be continued.

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This information was obtained from an article entitled "Government Indemnification of Contractors" written by Richard A. Smith in the NCMA Journal, Fall 1984.